

**Before the  
FEDERAL COMMUNICATIONS COMMISSION**  
Washington, D.C. 20554

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DA 95 - 604

In the Matter of	)	
	)	
Pacific Bell	)	Transmittal No. 1773
Tariff F.C.C. No. 128	)	
	)	
	)	
U S West	)	Transmittal No. 584
Tariff F.C.C. No. 5	)	
	)	CC Docket No. 94-157

**MEMORANDUM OPINION AND ORDER  
SUSPENDING RATES**

Adopted: March 24 , 1995; Released: March 24 , 1995

By the Chief, Tariff Division, Common Carrier Bureau:

**I. INTRODUCTION**

1. On January 20, 1995, Pacific Bell and US West filed the above-captioned transmittals to reflect the exogenous treatment of Statement of Financial Accounting Standard No. 106 (SFAS-106), "Employers Accounting for Postretirement Benefits Other Than Pensions." On February 6, 1995, MCI Telecommunications Corporation (MCI) filed a petition to suspend and investigate both transmittals. Pacific Bell and US West filed replies on February 16, 1995. For the reasons given below, we suspend the Pacific Bell and US West transmittals and include them in our investigation in CC Docket No. 94-157.<sup>1</sup>

**II. BACKGROUND**

2. The investigation in CC Docket No. 94-157 was initiated in December 1994 to consider the local exchange carriers' (LECs') requests for exogenous treatment of SFAS-106 costs. In that proceeding, a number of LECs sought to adjust their price cap index (PCI) levels to reflect implementation of SFAS-106 since the United States Court of Appeals decision in

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<sup>1</sup> Bell Atlantic Telephone Companies Tariff F.C.C. No. 1, Transmittal No. 690, et al, CC Docket No. 94-157, Memorandum Opinion and Order, DA 94-1613 (Com. Car. Bur., rel. Dec. 29, 1994) (SFAS-106 Suspension Order).

Southwestern Bell Telephone Company v. FCC, 28 F. 3d 165 (D.C.Cir. 1994). In that case, the United States Court of Appeals for the District of Columbia Circuit reversed and remanded a Commission Order which concluded that increases in booked Other Postretirement Employee Benefits (OPEB) costs caused by the implementation of SFAS-106 were not eligible for exogenous treatment.<sup>2</sup> SFAS-106 requires companies to account for OPEBs on an accrual basis, treating OPEBs as a form of deferred compensation earned by employees during their working years. Accordingly, the costs of OPEBs are recognized during the years the benefits are earned, rather than during the years when the amounts of benefits are actually paid by the company. In addition, SFAS-106 requires companies to recognize on their books the amount of their unfunded obligation for OPEBs to retirees and to active employees as of the date of their adoption of SFAS-106. This obligation is known as the Transitional Benefit Obligation (TBO).<sup>3</sup>

3. While it is clear that after the Southwestern Bell decision, supra, changes in LEC OPEB costs caused by the implementation of SFAS-106 are eligible for exogenous treatment, other issues remain that concern the specific adjustments that LECs may make to their PCI levels to reflect the cost change. Those issues are now under investigation in CC Docket No. 94-157.

### III. PLEADINGS

#### A. The Transmittals.

4. In Transmittal No. 1773, Pacific Bell proposes to increase its PCI to incorporate exogenous cost adjustments resulting from adoption of SFAS-106. Pacific Bell states that these adjustments are in addition to the increase in the PCI for the TBO in 1993.<sup>4</sup> Pacific Bell asserts that its proposed exogenous cost adjustment is temporary and is intended to recover the revenues it would have earned during the period between adoption of the OPEB Order and its reversal and remand. In addition, Pacific Bell is proposing increases to its PCI in an amount that reflects its on-going annual requirement for recovery of the incremental costs associated with the adoption of SFAS-106.<sup>5</sup> Pacific Bell states that these incremental costs are based on a number of

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<sup>2</sup> Treatment of Local Exchange Carrier Tariffs Implementing Statement of Financial Accounting Standards, "Employers' Accounting for Postretirement Benefits Other Than Pensions," CC Docket No. 92-101, Suspension and Investigation Order, 7 FCC Rcd 2724 (Com. Car. Bur. 1992), Memorandum Opinion and Order, 8 FCC Rcd 1024 (1993) (OPEB Order).

<sup>3</sup> TBOs were created as a result of both the change from cash-based to accrual accounting and the SFAS-106 requirement that companies recognize on their books the amount of their unfunded obligation for OPEBs to retirees and to active employees existing as of the date of their adoption of SFAS-106. This unfunded obligation reflects the amount that a company would have accrued on its books as of the effective date of the accounting change if it had been operating under the accrual method. SFAS-106 Suspension Order, at para. 7.

<sup>4</sup> Pacific Bell Transmittal No. 1773, Description and Justification (D&J) at 1.

<sup>5</sup> Id.

actuarial assumptions, including average age and number of retirees, rate of inflation for medical costs, and return on plan assets, i.e. the OPEB and Voluntary Employee Beneficiary Association (VEBA)<sup>6</sup> funds. Pacific Bell assumes that these funds are earning a return on investment of 9 and 8.5 percent respectively.<sup>7</sup>

5. US West proposes in Transmittal No. 584 to adjust its PCI to reflect the difference between the TBO portion SFAS-106 and the ongoing incremental costs of adopting SFAS-106.<sup>8</sup> US West states that it is seeking to reflect the difference between TBO exogenous cost treatment, already in its PCI, and the incremental OPEB costs that it may now submit for exogenous cost treatment based on the Southwestern Bell decision.<sup>9</sup> According to US West, these incremental OPEB costs were calculated using standard actuarial assumptions, including that its VEBA and OPEB fund obligations that were funded on December 31, 1992 are assumed to be earning a 9 percent and 8.5 return on investment, respectively.<sup>10</sup>

#### B. MCI's Petition

6. MCI filed a petition to suspend and investigate both the Pacific Bell and US West transmittals. MCI contends that the Commission's Responsible Accounting Official (RAO) Letter 24<sup>11</sup> bars Pacific Bell and US West from recovery of OPEBs until those costs are actually incurred.<sup>12</sup> According to MCI, the Commission has established that work force reduction costs should be recognized when they actually occur. MCI claims that Pacific Bell and US West are proposing to adjust their existing PCIs for exogenous work force costs they expect to incur in the future. Premature recognition of OPEBs will, according to MCI, allow both Pacific Bell and US West to raise their PCIs and realize more pricing flexibility, especially for raising prices, in monopoly access markets.<sup>13</sup> MCI objects to Pacific Bell's and US West's proposals to adjust their existing PCIs for costs they expect to incur in the future because it is difficult for a LEC

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<sup>6</sup> A VEBA fund is established by the employer to partially fund OPEB obligations.

<sup>7</sup> Pacific Bell D&J at Appendix "Direct Case filed by Pacific Bell in Suspension and Investigation Order," CC Docket No. 92-101 at 9.

<sup>8</sup> U S West Transmittal No. 584, D&J at 1-1.

<sup>9</sup> Id. at 1-2 to 1-3.

<sup>10</sup> Id. at 1-3 to 1-4.

<sup>11</sup> RAO Letter 24, "Accounting for Work Force Reduction Programs", 9 FCC Rcd 1676 (Com. Car. Bur., A and A Div. 1994) (RAO Letter 24).

<sup>12</sup> MCI Petition at 1-2

<sup>13</sup> Id. at 8.

to project accurately what its work force reduction expenses will be. Therefore, says MCI, the LECs should book their OPEB expenses, just as RAO Letter 24 requires, when the amounts have actually been funded. MCI contends that under this method, the LECs will be ensured of being compensated for actual OPEB expenses.<sup>14</sup>

7. MCI further argues that Pacific Bell and US West do not clearly state in their transmittals the basis for assuming their VEBA funds earns 8.5 percent interest and their OPEBs funds earns 9 percent interest. MCI contends that these companies have the ability to earn more than 9 percent on these funds.<sup>15</sup> In addition, MCI asks the Commission to review the amount of OPEBs cost Pacific Bell and US West allocated to nonregulated activities and to activities "subject-to-separations."<sup>16</sup> MCI next argues that even if the Commission does not apply RAO Letter 24 to OPEB expenses, the potential still exists for a "double-count" of OPEBs through the GNP-PI adjustment in the price cap formula.<sup>17</sup> Finally, says MCI, Pacific Bell and US West continue to rely on the same facts here to support OPEB exogenous cost treatment as they used to support OPEB costs currently under investigation in CC Docket No. 94-157. MCI argues that the Commission should therefore suspend and investigate these transmittals as well.<sup>18</sup>

### Replies

8. In their replies, Pacific Bell and US West contend that the Commission has ordered the use of SFAS-106 accrual accounting for OPEB costs and that RAO Letter 24 has no bearing on this requirement. According to Pacific Bell, RAO Letter 24 states that accounting for work force restructuring is an exception to the Commission policy that requires conformance with Generally Accepted Accounting Procedures and Part 32 of the Commission's rules, 47 C.F.R. Part 32.<sup>19</sup> US West states that it is accounting for OPEB costs in accordance with RAO Letter

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<sup>14</sup> Id.

<sup>15</sup> Id. at 10.

<sup>16</sup> MCI Petition at 10-11.

<sup>17</sup> GNP-PI refers to the Gross National Product Index minus a productivity factor. GNP-PI is used to calculate the annual PCI adjustment made by LECs to account for inflation in the economy. See Section 61.45 of the Commission's Rules, 47 C.F.R. § 61.45; Policy and Rules Concerning Rates for Dominant Carriers, Order on Reconsideration, 6 FCC Rcd 2637, 2641 (1991) (LEC Price Cap Reconsideration Order).

<sup>18</sup> MCI Petition at 12.

<sup>19</sup> Pacific Bell Reply at 2-3.

20<sup>20</sup> which provides specific guidance as to how the effects of SFAS-106 should be recorded on a carrier's books for regulatory purposes.<sup>21</sup> In addition, US West denies that its Transmittal No. 584 contains any costs classifiable as restructuring charges under RAO Letter 24. Rather, US West states, the SFAS-106 costs included in Transmittal No. 584 are the incremental costs of accruals which have been made on a routine basis in accordance with all applicable Commission accounting requirements.<sup>22</sup>

9. Pacific Bell and US West further contend that their projected returns on their respective VEBA and OPEB funds are generally accepted as reasonable projected returns on a mixed portfolio of major stocks and investment grade bonds.<sup>23</sup> US West maintains in addition that a 9 percent rate of return on SFAS-106 plan assets is appropriate and is used by other companies.<sup>24</sup> Pacific Bell and US West also state that they properly allocated the amount of OPEBs costs allocated to nonregulated activities and activities subject-to-separations.<sup>25</sup> In addition, U S West contends that its allocation of 5 percent of OPEB expenses to nonregulated operations comports with Part 64 of the Commission rules and, finally, that exogenous treatment of SFAS-106 costs will not result in double-counting through the GNP-PI adjustment in the price cap formula.<sup>26</sup>

#### IV. DISCUSSION

10. We have reviewed Pacific Bell Transmittal No. 1773 and US West Transmittal No. 584, supporting documents and pleadings. We find that the issues raised by these two transmittals are the same as the issues under investigation in CC Docket No. 94-157. As indicated above, Pacific Bell and US West state that they are proposing to revise their interstate access rates to reflect an adjustment of their exogenous costs for SFAS-106. While the Court has ordered the Commission to grant exogenous treatment of these postemployment benefits, the question of the specific amount eligible for exogenous treatment is subject to investigation in CC Docket No. 94-157. Therefore, we are suspending the two transmittals and including the issues presented therein in CC Docket No. 94-157.

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<sup>20</sup> RAO Letter 20, "Accounting for Work Force Reduction Programs," 9 FCC Rcd 1676 (Com. Car. Bur. Aand A Div. 1994).

<sup>21</sup> US West Reply at 3-4.

<sup>22</sup> Id.

<sup>23</sup> Pacific Bell Reply at 4; US West Reply at 4.

<sup>24</sup> US West Reply at 4.

<sup>25</sup> Pacific Bell Reply at 4; US West Reply at 4.

<sup>26</sup> US West Reply at 9-10.

## V. ORDERING CLAUSES

11. Accordingly, IT IS ORDERED that, pursuant to Section 204(a) of the Communications Act, 47 U.S.C. § 204(a), and Section 0.291 of the Commission's Rules, 47 C.F.R. § 0.291, the revised rates set forth in Pacific Bell Tariff F.C.C. No. 1, Transmittal No. 1773 and U S West Tariff F.C.C. No. 5, Transmittal No. 584 ARE SUSPENDED for one day from the current effective date and an investigation of those rates is included in CC Docket Nos. 94-157. Pacific Bell and U S West SHALL FILE supplements reflecting this suspension no later than five days from the release of this Order and should cite the "DA number" of this Order as the authority for making this tariff filing.

12. IT IS FURTHER ORDERED that, pursuant to Sections 4(i) and 204(a) of the Communications Act, 47 U.S.C. §§ 154(i), 204 (a), and Section 0.291 of the Commission's Rules, 47 C.F.R. § 0.291, Pacific Bell and U S West SHALL KEEP ACCURATE ACCOUNT of all amounts received that are associated with the rates that are the subject of this investigation.

13. IT IS FURTHER ORDERED that Pacific Bell and U S West SHALL INCLUDE STATEMENTS in all subsequent transmittals revising rates indicating whether, and to what extent, the price change is predicated upon the exogenous cost claim set forth in Transmittal Nos. 1773 and 584, respectively.<sup>27</sup>

14. IT IS FURTHER ORDERED that the petition to suspend and investigate Pacific Bell Transmittal No. 1773 and U S West Transmittal No. 584 filed by MCI Telecommunications Corporation IS GRANTED to the extent discussed above and otherwise IS DENIED.

FEDERAL COMMUNICATIONS COMMISSION



Geraldine A. Matise  
Chief, Tariff Division  
Common Carrier Bureau

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<sup>27</sup> We anticipate that any such transmittals will be suspended for one day, included in this investigation, and made subject to an accounting order.